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SENSITIVE
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DEPARTMENT FOR EUR/RUS, EEB/IFD/OIA (GOERTHERT, BUTLER), L/CID
(PEARSALL)

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TAGS: EINV KIDE ETRD ECON RS

SUBJECT: 2009 REPORT FOR RUSSIA ON INVESTMENT DISPUTES AND
EXPROPRIATION CLAIMS

REF: STATE 49477

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PROTECT ACCORDINGLY.

¶11. (U) Per reftel request, attached is post's draft 2009 Report for Russia on Investment Disputes and Expropriation Claims. We have also e-mailed to EUR/RUS and EEB/OIA the draft report as a Word document marked to show changes from the 2008 Report for Russia. Begin text of draft report:

¶12. (U) The United States Government is generally aware that many United States persons have outstanding Soviet-era or pre-Soviet-era claims against the Government of the Russian Federation. These claims are outside the reporting scope of the Act. While such claims are not included in this report, the Department of State provides appropriate assistance to all United States persons with claims against Russia.

¶13. (U) The United States Government is aware of six (6) reportable claims of United States persons against the Government of the Russian Federation. Only one of the Claimants (Claimant F) has contacted the Embassy and Consulates during the past year. There has been one new reportable case in the past year (Claimant F).

CLAIMANT A

¶14. (U) A. Claimant A. B. Year 1995. C. Claimant A is a U.S. corporation that holds a contract for a sport fishing enterprise. According to the Claimant, in 1993 it obtained exclusive fishing rights to the Varzina River on the Kola Peninsula in a contract with the Lovozero District Administration (the local authorities for that part of the Kola Peninsula). In January 1995, these authorities alleged that Claimant A failed to fulfill certain obligations and abruptly cancelled the contract. Armed police forcibly shut down Claimant's fishing camp.

¶15. (U) The authorities held a new tender and awarded the local fishing rights to a competing Finnish-Russian joint venture. A Russian court ruled that the dispute should be resolved by arbitration in Stockholm as stipulated in the original contract. An arbitration hearing was held in June and an October 1996 decision awarded Claimant A USD 940,000. Neither the district nor the Oblast (region) complied with the award, so in 1997 and 1998 Claimant A undertook a number of court actions seeking enforcement of the award. In December 1997, the Murmansk Oblast Arbitration Court ruled in favor of Claimant A and dismissed the Murmansk authorities' claim that Claimant A's business activities were illegal. In February 1998, the Murmansk Oblast Court ordered the recognition and enforcement of the Stockholm award. In March 1998, the Murmansk Authorities appealed to a higher Federal Arbitration Court in St.

Petersburg and the decision by the Murmansk Arbitration Court was overturned. The case was returned to the Murmansk Arbitration Court, which issued a writ of execution of the Stockholm Award. When local authorities again appealed, the Supreme Court of Russia rejected the appeal.

¶ 6. (U) The Murmansk administration then argued that the arbitration award was against the Lovozero administration and, because the Murmansk Oblast was not a party to the contract, it was not responsible for settling the award. In December 1998, Claimant A petitioned the Murmansk court to direct the Oblast to pay the writ of execution against Lovozero. The presiding judge refused to hear the petition. In February 1999 an appeal was filed with the Supreme Court, which returned the appeal without action on the basis that it had already ruled on the case and it was the responsibility of the court bailiffs to take the necessary steps for execution. On June 2 and again on November 24, 1999, the Lovozero District Court instructed the bailiffs to execute the judgment against both the Lovozero District and the Murmansk Oblast.

¶ 7. (U) Consulate General and Embassy personnel raised this issue at increasingly higher levels between 1998 and 2004. On September 29, 1999, the U.S. Ambassador and St. Petersburg Consul General raised the issue directly with Murmansk Governor Yevdokimov. The St. Petersburg Consul General also wrote to Governor Yevdokimov regarding the case on December 21, 1999. The Ambassador wrote twice to then Minister of Justice Chaika (on October 12, 1999, and June 7, 2000) to protest the lack of action by Russian bailiffs in enforcing the courts' judgments. The Charg d'Affaires also wrote to the Minister of Justice on December 29, 1999. The Ministry of Justice responded that bailiffs attempted to enforce the judgment against Lovozero District, but were able to impound only 463,152 rubles of property (approximately USD 18,526 according to July, 2006 exchange rate).

¶ 8. (U) In the first half of 2001, Claimant A, supported by the USG, made progress in extracting assurances that the Chief of the Moscow bailiffs would pursue complete and thorough local enforcement of all the previous rulings in Claimant A's favor. Preliminary rulings in 2000 and 2001 from local courts that challenged Claimant A's award were successfully overturned by the Russian Supreme Court in June 2001. Embassy personnel met with the Bailiffs' Service in December 2001, and were told enforcement was being held up by new court actions filed by the Lovozero District. The Russian Supreme Court again on January 22, 2002 ruled that there should be no more appeals and the judgment should be executed. In February 2002 Embassy personnel accompanied Claimant A to a meeting at the Federal Bailiffs' Service, where it was agreed that representatives of the Moscow Bailiffs' Service would travel to the Murmansk Oblast to instruct local bailiffs to execute the court actions. Further appeals by Murmansk Oblast to the Russian Supreme Court were denied in March 2002. In May 2002, the court actions still had not been enforced against Lovozero District, and the Bailiffs' Service reported that two other creditors of the district were ahead of Claimant A, and also that the Chief Bailiff of Murmansk Oblast had been dismissed. In June 2002, the St. Petersburg Consul General again raised the case with the Governor of Murmansk Oblast, stressing the need to resolve the case soon.

¶ 9. (U) The Ambassador met with the Minister of Justice in December 2002 to once again raise the lack of enforcement in this case. The Minister claimed that the Bailiffs' Service was unable to enforce the judgment because other appeals were ongoing at the time. Subsequent to that meeting, the local creditors allegedly in line ahead of Claimant A withdrew their claims in December 2002, opening the door for enforcement by the bailiffs of Claimant A's claims. After another letter from the Ambassador to the Minister of Justice in February 2003, and a meeting between the St. Petersburg Consulate General and the Deputy Regional Presidential Representative in April 2003, Claimant A reported that the local administration had finally decided to allow recovery of the award and the local bailiffs were in the process of recovery; however, this did not occur.

¶ 10. (U) In January 2004 the local bailiff system unilaterally dismissed the case. Claimant A has not appealed this decision. Given the poor financial situation of the local administration, it was unlikely that Claimant A would be able to recover the entire amount

of its award from the Lovozero District.

¶11. (U) The Ambassador wrote again to the Murmansk Governor in September 2004, and subsequently received a reply that provided new justifications for not enforcing the decision and which made no effort to resolve the case. While the Embassy and Consulate General St. Petersburg continue to monitor the case, they have not been contacted by Claimant A since 2004.

CLAIMANT B

¶12. (U) A. Claimant B. B. Year 2000. C. Claimant B is a U.S. manufacturer of piezo quartz glass, used in electronic applications.

In 1994, Claimant B purchased part ownership in a quartz glass production facility in Gus-Khrustalniy in Vladimir Oblast. The quartz glass company subsequently went into bankruptcy. According to the Claimant, it secured a long-term lease on the company's equipment in 1997 and invested a significant amount of money (by some accounts as much as USD 7 million) in renovating the plant and re-starting production. In May 2000, the Vladimir Oblast prosecutor, acting for the Russian partners of Claimant B, filed a case challenging the validity of Claimant B's lease, for which Claimant B had completed its payments. On February 9, 2001, a Vladimir court ruled Claimant B's lease was invalid, and ordered the bankrupt glass company to repay USD 1.68 million to Claimant B. The other partners in the bankrupt enterprise used the court's orders to evict Claimant B from the quartz glass production facility in June 2001 and seized USD 1.2 million in inventory and work in progress. Claimant B appealed and subsequently lost two cases before the Nizhniy Novgorod appeals court, but won one case in June 2002. These decisions have let stand the invalidation of the lease and have invalidated the order for the bankrupt glass company to repay Claimant B for the lease, but have reaffirmed Claimant B's rights to inventory, equipment, and improvements in the disputed plant. One aspect of concern to Claimant B is that although local bailiffs have enforced rulings unfavorable to Claimant B, they have been unwilling to enforce rulings that reaffirm Claimant B's property rights.

¶13. (U) The Ambassador and other Embassy officials have raised this issue with the Ministry of Economic Development and Trade, the Prime

Minister's Chief of Staff and Ombudsman, the office of the Presidential Representative for the Central District, and other senior Russian government officials. The Ambassador also highlighted this issue in a May 2002 article for a leading Russian business publication. USG officials have also raised this issue with President Putin. The Ambassador traveled to Vladimir region in June 2002 to encourage a negotiated resolution.

¶14. (U) In June 2003, the Ambassador met with the Vice Governor of Vladimir Oblast, who promised to help broker a solution. The Oblast Government contacted a Swedish businessman to investigate the dispute, but did not succeed in resolving it. In October 2004, Claimant B's Russian assets were transferred to a new U.S. legal entity established by the firm's president when he left in June 2004. The new entity continued to pursue settlement of this dispute, and Claimant B informed the Embassy that there had been no progress toward resolution. Claimant B has not contacted the Embassy in more than two years, but the Embassy will continue to monitor the case and provide all appropriate assistance to Claimant B.

CLAIMANT C

¶15. (U) A. Claimant C. B. Year 2001. C. Claimant C is a venture capital firm that in April 2000 entered into a joint venture with a state-owned coal producer in Primorye Kray to produce germanium by burning special coals. According to the Claimant, it invested USD 5.5 million in equipment, improvements, and working capital in the venture. In November 2001, the Ministry of Energy informed Claimant C's joint venture partner that they should abrogate their contract with Claimant C and return the investment. Subsequently, Claimant C's joint venture partner lost its mining license and stated it was unable to repay the invested funds. Meanwhile, another company had

been given the mining license for the special coal deposit. Claimant C attempted to re-start the joint venture with the new company, but this new licensee did not show interest in negotiation and demanded an extremely large sum from Claimant C for transfer of the license. Because of the location and type of equipment, Claimant C believed it was unlikely that it could recover any significant portion of its investment through salvage.

¶16. (U) The Embassy and Department of Commerce officials have raised this issue in bilateral consultations with the Ministry of Economic Development and Trade, and have requested explanations from the Ministry of Energy. However, the Embassy has not heard from the GOR on this issue since November 2001, and the investor has not requested further assistance from the Embassy.

CLAIMANT D

¶17. (U) A. Claimant D. B. Year 2000. C. Claimant D is an investment company that originally bought a 20 percent minority share in a grain-processing company in the Russian Far East for USD 2 million. Claimant D also exported grain to the Russian firm in which it was a shareholder. According to the Claimant, following the 1998 financial crisis in Russia, the Russian firm was unable to pay Claimant D for the grain exports. In 2000, Claimant D found that it had been removed from the company board, was unable to access the company books, and the grain exports, held as collateral, were illegally removed from their silos. Claimant D in 2001 obtained two international arbitration awards totaling USD 3.7 million against the Russian company. In early 2002, Claimant D informed the Consulate General in Vladivostok that it had reached a compromise to recover its investment; however, the Russian company failed to make the agreed-upon payments. One of the Russian company's other creditors petitioned for bankruptcy in March 2002. Claimant D obtained a court order to freeze the Russian company's assets. However, during a brief interim when the parties had completed a negotiated settlement, the Russian company was able to sell its largest asset, a flour mill in Ussuriysk. Subsequently, the local representative of Claimant D had her automobile windows smashed and was threatened with physical violence. Claimant D pursued court action to reverse these asset sales, but in mid-June 2002 local courts refused to overturn the Russian company's asset sales.

¶18. (U) In August 2002 Claimant D received favorable court judgments freezing the sale of remaining assets of the grain-processing company and reaffirming the legitimacy of its arbitration award. Bankruptcy proceedings were initiated in November 2002 to determine the grain-processing company's liabilities and assets. At the request of the Vladivostok Consulate General and the Embassy, the Primorye Administration met with Claimant D in November and December

¶2002. The Ambassador wrote the Primoriye Governor in February 2003 urging resolution of this dispute. To date, the Governor has not responded. Another meeting between the two sides was scheduled for spring 2003, but did not occur. The DCM also raised the dispute directly with the local administration during a trip to Vladivostok in spring 2003. The Economic Minister Counselor met with local officials in April 2004. The investor has not requested further specific Embassy assistance within the past three years.

CLAIMANT E

¶19. (U) A. Claimant E. B. Year 2003. C. Claimants E are American citizens who held share-related rights in a major Russian corporation. They have filed suit in U.S. federal court against the Russian government and others, alleging that defendants expropriated their interests. Claimants approached the Department with a request for USG support of their case during the summer of 2008. The suit is pending, and the Department continues to monitor developments.

CLAIMANT F

¶20. (U) A. Claimant F. B. Year 2008. C. Claimant F is a partner in a

closed Russian joint stock company that was established in 1994 as a 50-50 Russian-American joint venture. Each side separately contributed approximately \$1 million in fixed assets, equipment and working capital in order to commence initial operations of the port of SovGavan, which is located in the Khabarovskiy Kray region of the Russian Far East. Between 1994 and 2007, virtually all of the joint venture's earnings were reinvested in the corporate entity and used to improve the site's infrastructure, including adding rail spurs, paving storage areas, and improving the facility's electrical supply. As the volume of cargoes shipped through the facility increased, approximately \$1.5 million of additional operating equipment (cranes, frontend wheeled loaders, and hydraulic logs loaders) were added, most of which was either financed by or leased from Claimant F. In the summer of 2007, the joint stock company received a firm offer of \$1.1 million for its fixed assets. Claimant F considered that offer to be unacceptably low.

¶21. (U) Since its founding in 1994, the joint stock company had exclusive operating rights at the ten-hectare port facility, which it had continually leased from another open Russian joint stock company (hereinafter referred to as the "Lessor"). In 2000, Claimant F acquired 36% of the Lessor's publicly traded stock. Subsequently, the original joint stock company and the Lessor signed a 20-year long term lease agreement for the entire site. Claimant F maintains that the long-term lease is the Lessor's sole asset.

¶22. (U) In early 2008, the Lessor forcefully took over all of the original company's assets and began operating the facility independently itself. Initially, the takeover did not involve any court or other legal procedure. Instead, overnight, the original company's security forces were replaced; proceeds from the original company's operations (e.g., the accumulated accounts receivable) were diverted to the Lessor's bank account; and the original company's employees were hired by the Lessor; the original company's fixed assets and operating equipment at the port were seized, along with all of the original company's operating supplies, spare parts and pre-paid expenses. In addition, according to Claimant F, as the Lessor lacked any authority or legal status necessary to legally operate the port, the Lessor also misappropriated the original company's official stamps and, by forging the original company's signature authority, utilized the stamps to illegally operate under the original company's permits, licenses and contracts with the Russian Federal Customs Service, the Russian Maritime Security Service, and with railroad and electrical utility service providers.

¶23. (U) The regional government administration of Khabarovskiy Kray (the administrative region of the Russian Far East where the port is located), as well as regional and local prosecutors, police and court officials, were informed of the takeover by Claimant F and its Russian lawyers through official filings, written updates and numerous meetings. However, none of these regional and local officials took any action or intervened to stop the takeover of the port. Claimant F also informed Russian Customs and the Russian Maritime Security Services of the takeover.

¶24. (U) Since the takeover, the U.S. Consul General in Vladivostok has been very actively involved in advocating for the claimant's rights with regional and local officials, but those efforts have also been ignored.

¶25. (U) In August 2008, the Lessor forced the original company into bankruptcy, and the original company is now in the final liquidation stages of the official bankruptcy process. During the period when the Lessor freely used the port's equipment, most of it was destroyed, and its value today is minimal, according to Claimant F. It also appears that the bankruptcy trustee, who was nominated by the Lessor, will avoid filing a \$1.5 million civil damages claim against the Lessor for the misappropriated port assets and equipment despite strong evidence of the theft. Claimant F has no legal standing or status in the bankruptcy proceeding.

¶26. (U) The bankruptcy proceeding has also placed Claimant F's 36% ownership position in the Lessor in serious jeopardy. The Lessor has closed the port facility and plans to lay off all but two employees. The Lessor is now financially viable only because of loans from its majority owner, none of which have been reviewed or

approved by the board of directors or shareholders. Claimant F believes that the replacement value of the port facility is over \$10 million but, in the current depressed economic conditions in the Russian Far East, it might sell for approximately \$4 million. The Embassy and Consulate General in Vladivostok will continue to monitor the case and provide all appropriate assistance to Claimant F.

IDENTITY OF CLAIMANTS

127. (SBU) The Claimants are identified as follows:

Claimant A: Kola Salmon Marketing Inc.
U.S. Citizen
No Privacy Act Waiver

Claimant B: Russian Quartz, Ltd. (Formerly Sawyer Research Products)
U.S. Citizen
No Privacy Act Waiver

Claimant C: Pennwood Industrial Products
U.S. Citizen
No Privacy Act Waiver

Claimant D: Euro Asian Investment Holding, Inc.
U.S. Citizen
No Privacy Act Waiver

Claimant E: U.S. Investors in the Yukos Oil Company
U.S. Citizens
No Privacy Act Waiver

Claimant F: Global Forestry Management Group
U.S. Citizen
No Privacy Act Waiver

BEYRLE